



VENABLE

Dealing with Nonprofit Donors: Risks, Restrictions, and When to Say “No Thanks”

Thursday, March 30, 2017, 12:30 pm – 2:00 pm ET

Venable LLP, Washington, DC

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- **April 26, 2017:** [Government Investigations and Controversies: Key Legal and Communications Strategies for Nonprofits to Prepare for and Manage the Crisis](#)
- **May 18, 2017:** [Moving Money Overseas and Back: What Every Nonprofit Operating Internationally Needs to Know](#)
- **June 13, 2017:** [An Independent Contractor, an Employee, and Their Attorney Walk into a Bar: Why This Is No Joke for a Nonprofit](#)



Recent News Stories Highlight Donor Issues

- Presidential foundations
 - Identity of donors
 - “Pay to play”
- Association with donor becomes embarrassing
- Fraudulent conveyance cases – donor hides assets from creditors by transferring to charity
- “Naming” cases



Challenges in Dealing with Donors

- Attracting donors while protecting the institution
- Donor intent (restrictions) versus charity needs and purposes
- Protecting donor privacy versus public accountability
- Impossible to predict future events



Donor Restrictions – Basic Concerns

- Impact of restriction on charitable deduction
- Impact of restriction on nonprofit's tax-exempt status
- Acceptable versus unacceptable restrictions
- Modifying a restriction
- Accounting impact of restriction
- Red flags indicating problems



Common Gift Restrictions

- Restricted purpose of gift
- Investment restrictions
- Holding period: Ability to sell or transfer gift
- Endowment: Invasion of principal
- Naming
- Retained right to use property
- Right to advise on disposition of gift



Some Basic Concerns

- Availability of charitable deduction if restrictions are too severe
 - Has donor really made a gift?
- Accounting issues
 - Unrestricted, temporarily restricted, permanently restricted
- Impact of restriction on tax-exempt status
 - Private inurement
 - Private benefit
- Getting “sideways” with the donor
- Potential embarrassment associated with restriction



Acceptable Restrictions

- Naming
- Specify charitable purpose (consistent with charity's needs)
- Reasonable holding period – important to achievement of charitable purposes
- “Incidental” benefits to donor
- Donor advised fund



Unacceptable Restrictions

- Continued control of the asset by donor
- Retained right to direct distribution
- Transfer of asset subject to excessive liabilities
- Inability of charity to dispose of asset
- Requirement to use gift to benefit donor or relative of donor
- Retained use of asset by donor
- Commercial benefit to donor



Modifying a Restriction – Uniform Prudent Management of Institutional Funds Act (UPMIFA)

- UPMIFA permits deviation (in management, investment, or purpose)
 - With donor consent
 - With court and state Attorney General approval
 - UPMIFA permits prudent “appropriation” of an endowment fund



Some Red Flags

- Restriction is inconsistent with charitable purpose
- Donor benefits from restriction in some way
- “Unknown” donor shows up on December 31
- Inability to dispose of asset
- “Difficult” assets
- Donor is charity shopping/charitable intent questionable



Developments in Donor Privacy

- List of contributors (IRS Form 990 Schedule B) generally does not need to be disclosed publicly
- Exception for gifts to private foundations
- States seeking to force disclosure (e.g., California)
- Judge's order regarding Harvard donor



Techniques for Preserving Donor Privacy

- Require confidentiality agreements for employees of nonprofits
- Use of donor advised funds
- Written and publicly shared donor privacy policies



Gift Acceptance Policies

- Establish prospectively to guide the organization in soliciting, procuring, and “closing” gifts
- Policy should govern both *acceptance* and *disposition* of gifted property
 - In many instances, the true “value” of a gift is in the proceeds that arise upon disposition
- Helps in managing donors
 - Gives way to say “no thanks”



General Comments

- No specific rules or laws directly on point
- Gift policies are not required; rather, part of “best practices”
- Policy should “fit” the organization and reflect a workable and helpful process
- Often used as an aid to saying “no”



Sample Structure of Gift Policy

- Statement of mission, values, guiding principles, and organizational priorities
- Overview of different types of gifts and criteria for acceptance and disposition
- Procedural and administrative matters



Internal Governance

- Gift Acceptance Committee
 - Trigger: Gift amount and types requiring review and approval
 - Composition: Just directors, or other professionals and volunteers too?
 - Authority: Able to take action on behalf of the organization or in an advisory capacity to the Board?
 - Consistent with organization's bylaws?
 - Signature authority?



Internal Governance (cont'd)

- Tax considerations:
 - Any effect on Section 501(c)(3) status?
 - Private foundations: Ensure compliance with Internal Revenue Code Chapter 42 rules
 - Unrelated business income tax (UBIT) implications?
 - Acceptance of interests in LLCs or other pass-through entities
 - S corporation stock



Specific Types of Gifted Property

- Cash
- Securities – marketable versus non-marketable, length of time held by donor
 - UBIT
 - Limitations on disposition
- Real estate
 - Due diligence: Phase I environmental survey; appraisal
 - Consider use of single-member, disregarded LLC to accept donation
- Tangible personal property
 - Expected use
 - Anticipated costs



Specific Types of Gifted Property (cont'd)

- Intellectual property
- Conservation easements and façade easements
- Gifts of property with expected disposition within three years
- Life-income gifts: special asset-type considerations can apply



Protecting the Charity

- Due diligence on donor
 - Newspaper reports
 - Internet research
 - Staff or contracted research firm
 - Gut check
 - Other
- Due diligence on contributed asset



Protecting the Charity (cont'd)

- Assets carrying potential for liability:
 - Real Estate
 - Environmental
 - Mortgage or other lien
 - Operating Businesses – Pending or potential claims
 - Partnership Interests – Know what assets the partnership holds



Liability Protection Techniques

- Environmental surveys
- Insurance
- Indemnification from donor
- Use of subsidiary to hold “risky” assets
 - Single-member, disregarded LLC
 - Supporting organization
 - Title-holding company
- Provide in gift agreement that UBIT will be paid from contributed assets



Steps When Discovering a Problem

- Option 1 – Do nothing. Distance is good.
- Option 2 – Be more proactive:
 - Get a complete explanation
 - Return donation?
- Option 3 – Help craft a solution



Steps When Discovering a Problem (cont'd)

- Address preemptively in donor privacy policy and gift agreements
- Consider getting public relations help
- Have talking points for the press and other inquiries
- Consider going to governmental authorities



Gift Agreement Provisions

- Relationship of Parties
- Confidentiality
- Termination Provision
- Variance Power
- Consider “Bad Boy” Clause



Questions?

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